Legislative Analysis

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COST-EFFECTIVE GOVERNMENTAL ENERGY USE ACT

House Bill 5727
Sponsor: Rep. Joe Haveman
Committee: Energy and Technology

Complete to 9-10-12

A SUMMARY OF HOUSE BILL 5727 AS INTRODUCED 6-6-12

House Bill 5727 would create the Cost-Effective Governmental Energy Use Act to encourage the use of energy performance contracts (EPC) by state and local governmental units. The objective of an EPC would be to implement cost-savings measures and achievement of both utility cost savings and operation and maintenance cost savings.

Generally speaking, "energy performance contracting," or EPC, refers to an agreement with an energy service company (ESCO) in which the ESCO, after conducting an energy audit, makes recommendations and provides all the services necessary to implement energy-saving measures. The project is typically financed by the savings realized when the energy saving upgrades are completed. If the actual savings fall short of what is needed to cover the costs of the project, the EPC—under a project savings guarantee—requires the ESCO to make up the difference between the savings realized and the cost of project financing for the life of the project.

Significant elements of the bill include the following:

- Require each governmental unit to implement cost-effective energy conservation improvements and maintain efficient operation of its facilities to minimize energy consumption and related environmental impacts and reduce operating costs.

- Specify that an "energy performance contract" (EPC) is the preferred method for completing energy audits and implementing cost-savings measures. The term would refer to a contract between a governmental unit and a "qualified energy service provider" for evaluation, recommendation, and implementation of one or more cost-savings measures. It could be structured as either a "guaranteed energy savings contract" or a "shared energy contract." Each of those terms would be defined in the bill.

- Require an EPC to require the qualified service provider to provide to the governmental unit an annual reconciliation of the guaranteed energy cost savings. Under the EPC, the qualified provider would be liable for any shortfall if the reconciliation revealed a shortfall in annual energy cost savings. An excess in annual energy cost savings could be used to cover potential energy cost-savings shortages in subsequent contract years. The EPC could provide that the reconciliation of amounts owed under the contract occur less frequently than annually, with final reconciliation occurring within the term of the EPC.

- Limit the term of an EPC to no longer than 15 years, though the term could also reflect the useful life of the cost-savings measures.

- Restrict an EPC contract for more than one year to only those projects in which the amount the governmental unit will spend on the cost-saving measures would not exceed the amount to be saved in energy, water, wastewater, and operating costs over 25 years from the date of installation.

- Require (with some exceptions) the qualified energy service provider, during the term of an EPC, to monitor certain reductions in energy consumption and the cost savings attributable to the cost-savings measures implemented under the EPC and provide the governmental unit with at least an annual report.

- Require the cost-saving measures under an EPC to comply with state or local building codes.

- Assign the Department of Technology, Management, and Budget as the lead agency and assign certain tasks to the department, including assembling a list of "qualified energy service providers" (as defined and specified in the bill); developing a standardized EPC process and standard EPC documents as detailed in the bill; developing an annual report to be presented to the legislative appropriation committees as specified in the bill; and assisting governmental units in identifying, evaluating, and implementing cost-savings measures at their facilities.

- Allow the department to charge a governmental unit a reasonable fee, not to exceed the lesser of $300,000 or 2 percent of the total cost of the EPC project, for administrative support and resources provided by the department. A governmental unit could add these fees to the total cost of an EPC.

- Allow a governmental unit to use designated funds, bonds, or master lease for any EPC, including purchases using installment payment contracts or lease purchase agreements if those uses were consistent with the purpose of the appropriation. In addition, unless otherwise provided by law or ordinance, the unit could also use funds designated for operating and capital expenditures or utilities.

- Allow a guaranteed energy savings contract to provide for financing by a third party, including tax-exempt financing. If done under a separate contract, the third-party financier could not be granted rights or privileges exceeding those available to the contractor under the guaranteed energy savings contract.

FISCAL IMPACT:

House Bill 5727 would require all governmental units to implement cost-effective energy conservation improvements to reduce energy consumption and environmental impacts and reduce operating costs. The bill specifies that energy performance contracts (EPCs) are the preferred method for completing energy audits and implementing cost-saving measures. The Department of Technology, Management, and Budget (DTMB) would serve as the lead agency for the development and promotion of EPCs in governmental units.

The basic premise of EPCs is to accomplish energy savings projects without high up-front capital costs. Qualified energy service providers conduct a comprehensive energy audit of the governmental unit facility and identify improvements to save energy. The qualified energy service provider then designs and constructs a project that meets the governmental unit's needs and arranges the necessary funding. The qualified energy service provider guarantees (assumes risk of project success or failure) the energy cost savings and operation and maintenance costs savings. After the project ends, the additional cost savings accrue to the governmental unit.

Under the bill, governmental units would be required to implement certain energy saving measures, preferably through EPCs. EPCs could be structured as either a guaranteed energy savings contract or a shared energy savings contract (definitions are provided above and in the bill). In both instances, energy savings are captured that would meet or exceed the cost of implementing the energy saving measures over the long term.

Specific savings to governmental units cannot be estimated, but would likely be positive as compared to the current baseline over the long term. The savings would be realized from reduced utility costs as well as reduced operation and maintenance costs outweighing the cost of the energy saving measures implemented. The bill provides provisions that would attempt to ensure that authorized projects realize overall savings that exceed overall costs for the governmental unit. The bill would require an EPC to provide that the qualified energy service provider would be liable for any shortfall if the annual reconciliation revealed a shortfall in annual energy cost savings determined in the contract. Conversely, if the reconciliation showed an excess in annual energy cost savings, the excess savings could be used to cover potential energy cost-savings shortages in subsequent contract years. The bill also states that a governmental unit shall not enter into an EPC for a period of more than 1 year unless the governmental unit finds that the amount it would spend on the cost-saving measures would not exceed the amount to be saved over 25 years from the date of installation.

DTMB would realize certain administrative cost increases under the provisions of the bill. (DTMB responsibilities are highlighted in the the summary above.) However, many of the costs associated with the bill would be offset by the provision allowing DTMB to charge a reasonable fee that would not exceed the lesser of $300,000 or 2% of the total cost of the EPC.

Under Public Act 122 of 1987, the State of Michigan has implemented multi-year, performance contracts to accomplish energy efficiency measures in state-owned buildings. The Michigan Energy Office (MEO) and DTMB Acquisition Services have assisted state agencies with performance contracting processes. Since the passage of the legislation, the State of Michigan has realized approximately $5.0 million in net savings.

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